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March 3, 2000

The Honorable Tom Bliley, Chairman
Committee on Commerce
U.S. House of Representatives
2125 Rayburn House Office Building
Washington, D.C. 20515

Dear Mr. Chairman:

As the full House Commerce Committee prepares to markup electricity restructuring legislation, we want to reiterate Enron's strong support for Congressional enactment of federal legislation to address the real problems occurring in today's wholesale electricity market. There is an urgent need to pass legislation to ensure healthy wholesale competition and to increase reliability. Unfortunately, H.R. 2944 as currently drafted does not accomplish its stated goals.

As the largest marketer of wholesale gas and electricity, Enron can only support H.R. 2944 if it is amended to allow all competitors fair and equal access to the interstate monopoly transmission network. Simply put: the interstate commerce clause must apply to interstate transmission. Today, utilities use their preferential access to transmission lines to favor themselves and to discriminate against competitors. This alone impedes fair market competition.

The attached position paper outlines several needed bill improvements. Of these, the most critical is to require all uses of our nation's transmission lines, whether used by the transmission owners or by others, to be under the same rates, terms and conditions of the same tariff and for all utilities to separate their transmission and sales functions to remove their incentive to discriminate against competitors. The same transmission rates, terms and conditions of the same tariff should apply to both wholesale and retail transactions regardless of whether a state has "unbundled" its retail market. This type of essential equal access requirement already applies to our nation's other interstate network systems such as natural gas pipelines, long distance telephone lines, and air traffic control systems.

We ask you to support a more competitive electricity market and get the rules right as we enter the 21st century. We thank you for your support, and we would be pleased to further discuss this important issue with you at your convenience.

Sincerely,

Cynthia C. Sandherr

cc: House Republican and Democrat Leadership
House Commerce Committee Members

Enclosure

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MEMORANDUM

February 1, 2000

RE: Enron Corp. Comments on H.R. 2944, "Electricity Competition and Reliability Act," as reported from the Subcommittee on Energy and Power on October 27, 1999

1. Transmission Service

A. ***Equal Transmission Access for All Users and Separation of Functions*** . The FERC's requirement, in Orders No. 888 and No. 889, that the marketing function of utilities be separated from and deal at arms-length with utilities' transmission operations, has helped to reduce preferential treatment to utilities' marketing activities. However, the FERC's orders apply only to utility wholesale sales and to "unbundled" retail service (*i.e.*, the separate provision of generation, transmission, and distribution services to a customer). With respect to the transmission component of bundled retail service, there is no requirement that utilities charge themselves the same rate, observe the same priorities, reserve transmission through an OASIS, or observe the restrictions on the flow of information between employees engaged in the "transmission" and "sales" functions.

Since the vast majority of the U.S. utility sales (approximately 80%) still consist of bundled retail service, the result of this limited application of open access is that utilities are able to interfere with the proper working of both the wholesale and retail markets, by taking unfair advantage of this loophole. As described in detail in the "Petition for Rulemaking on Electric Power Industry Structure and Commercial Practices" submitted to the FERC by Enron and others industry participants, the retail merchant component of vertically integrated utilities has unfettered access to non-public information about activities on the utility's transmission system and is able to schedule and curtail transmission relating to bundled retail sales without any of the competitive safeguards required of wholesale sales and FERC-regulated transmission. As a result, utilities are able to "game" and manipulate the system so that the open-access, transparent, and non-discriminatory regime envisaged in Order No. 888 is confined to a small fraction of electric power transactions. Finally, while it is likely that FERC Order No. 2000 will reduce some transmission-related barriers to competition, it does not grant FERC any additional authority to regulate the transmission component of bundled retail sales and thus does not obviate the need for corrective action.

As was learned when these same issues were addressed in the natural gas pipeline industry, meaningful competition flourished only after transmission owners were required fully to unbundle the transmission and sales components of service and to offer the same transmission rates and terms to all customers, regardless of whether the transmission service was part of a bundled sale or a stand-alone transmission service. That experience indicates that, other than requiring separate ownership of merchant and transmission functions, the only way to eliminate the ability of vertically integrated utilities to obtain unfair advantages in competitive markets is to subject the merchant function, at both the wholesale and retail level, to the same transmission rates, terms and conditions, and procedures for reserving transmission capacity, as apply to unaffiliated users of the system. The analog in the electric power industry to what the FERC did in its Order No. 636 is to (1) require that all retail service providers, including vertically integrated utilities providing bundled retail service, purchase and schedule transmission services under the same open access tariff as is available to other, non-affiliated users, (2) require that all transmission service be offered, purchased and scheduled under a uniform, open access transmission tariff, under which all users pay the same rates for the same services, pursuant to the OASIS that the FERC has mandated for wholesale transmission transactions, and (3) require vertically integrated utilities to separate their business functions, in a manner similar to the separation of transportation and sales functions under Order No. 636 applicable to gas pipelines.

H.R. 2944, as reported by the Subcommittee on October 27, 1999 (the "Bill") takes the opposite position in that it codifies the FERC's incorrect decision not to extend federal open access policies to apply to the transmission component of bundled retail sales. Section 101(b)(2)(B) amends the Federal Power Act to deny FERC jurisdiction over "the transmission of any bundled retail sale of electric energy." For the reasons stated above, this change goes in the wrong direction and will significantly decrease the extent to which competition can work to reduce the cost of electricity. It will also perpetuate the present approach under Order No. 888, which enables transmission owning utilities to favor their own generation with respect to the vast majority of their activities and to manipulate the energy commodity markets to their own advantage.

Instead of this approach, FERC's transmission jurisdiction should be clarified so as to include all transmission (not just wholesale and unbundled retail). FERC should be directed to require all utilities to put <u>all</u> uses of the transmission system under the same open access tariff and subject to the Order No. 888 and 889 requirements. All scheduling and curtailment would thus be done on a nondiscriminatory, transparent, open access basis. These requirements should apply to all transmission owners, including power marketing administrations, municipals, and cooperatives.

Further, in order to eliminate discrimination and enhance competition in both wholesale and retail markets, the legislation should direct FERC to issue a final rule within 180 days to require all utilities to separate their various business functions. At a minimum, a utility would be required to separate its transmission and distribution functions from its sales function.

An amendment to the Federal Power Act stating that FERC has jurisdiction over all interstate transmission of electricity, irrespective of when or whether it becomes bundled with a retail sale of the electricity, would also be helpful in resolving confusion that was recently exacerbated by a decision of the United States Court of Appeals for the Eighth Circuit. In its Order No. 888, FERC attempted to rationalize its failure to apply its open-access requirements to bundled transmission by asserting, we submit, wrongly, that it lacked jurisdiction over interstate transmission when the owner bundles it with a retail sale. Taking FERC's rationalization at face value, the Eighth Circuit in *Northern States Power v. FERC*, 176 F.3d 1090 (8th Cir. 1999), held that FERC did not have jurisdiction to require that the same transmission curtailment rules apply to all firm reservations of transmission service and that Northern States was free to discriminate against third parties' uses of Northern States' transmission system, ignoring that, as explained below, those other uses are needed to serve end-use consumers in other states. Explicitly affirming FERC's authority to eliminate discrimination from all interstate electricity transmission would eliminate this harmful precedent.

We are aware that some advocates have expressed concerns that such an approach could have an impact on the ability of utilities to continue to serve their native load customers. We believe these concerns are not well founded. First, most transmission providers are already obligated by their state regulators to plan and construct the facilities needed to provide adequate service. Moreover, Order No. 888 already requires transmission providers to add additional transmission facilities needed to provide transmission service for which a request for transmission service has been received. This requirement is codified and amplified in Section 105 of the Bill, which authorizes the FERC to order a transmitting utility to "enlarge, extend, or improve" its transmission facilities, unless it cannot, after making a good faith effort, obtain necessary approvals or property rights. By complying with these state and federal obligations, transmission providers will avoid having to choose between providing reliable service to native load customers that obtain their power supply from the transmitting utility's merchant function and native load customers that choose to obtain their power supply from a different provider.

We note that the electric industry does not condone failure by utilities to adhere to their contractual obligations, even if the utility's actions are intended to prevent disruptions to native load. For example, as widely reported in the trade press, during the last week of July 1999, Cinergy apparently violated the East Central Area Reliability Coordination Agreement by improperly drawing power it did not own from the interchange to meet its own supply obligations.[1] The trade press

1 Electric Utility Week, November 29, 1999, "New Revelations About Cinergy's July Actions Prompt Condemnation."

reported that violation of these requirements made the grid more vulnerable to blackouts and threatened to damage electric equipment on the grid's infrastructure.[2] The point is that electric industry standards do not permit utilities to violate their commitments, even if adhering to commitments can result in curtailments of native load. By conforming to industry planning and operating standards, utilities can protect their native load customers, their interconnected utilities, and their transmission customers from harm while adhering to their contractual obligations to wholesale transmission customers. Placing all transmission under FERC jurisdiction will thus not mandate any different type of commitment than is already required to maintain system reliability.[3]

It is important to recognize the harmful effect that divided federal and state regulation have on electricity service reliability and efficiency. Today's power industry is not composed of stand-alone electric utility companies operating independently of each other within their respective states. Rather, power grids are operated on an interconnected basis that makes it possible, indeed necessary, for each utility to share transmission and generation resources, including redundant resources essential to reliability, in order to provide reliable service most economically.

Beginning in the 1960s, the industry, with the encouragement of the Federal Power Commission, responded to dramatic and highly publicized power failures in New York and other metropolitan areas by encouraging regional interconnections to increase reliability and to reduce costs. It was widely recognized that a more tightly coordinated and integrated grid connected to a greater number of generating resources throughout large regions would be less susceptible to the types of equipment failures or human errors that caused those power failures.[4]

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2 Dow Jones Energy Service, November 23, 1999, "Cinergy Leeched Power During Summer Price Spikes."

3 In this regard, we further note that Congress has enacted an amendment to the Federal Power Act which prohibits discrimination against wholesale customers in favor of retail customers during shortages of electric energy or capacity. Section 202(g) of the Federal Power Act, which was added by Section 206 of PURPA, was intended to prevent utilities from discriminating against wholesale customers during periods of shortage of energy or capacity in circumstances which, from a quality of service perspective, are identical to those associated with shortages of transmission capacity. Section 206 mandates that, "[i]n order to insure continuity of service to customers of public utilities," the FERC must, by rule, require public utilities, among other things, to "accommodate any [shortages of electric energy or capacity which would affect a utility's capability of serving its wholesale customers] in a manner which shall . . . provide that all persons served directly or indirectly by such public utility will be treated, (sic) without undue prejudice or disadvantage." An approach under which all transmission (including the transmission component of bundled retail service) is subject to FERC jurisdiction, under which the FERC has a similar obligation with respect to shortages of transmission capacity, with the proviso that transmission providers have the "first call" to reserve capacity for native load, would not impose any unreasonable obligation on transmission providers. Such an approach is necessary to insure that customers of competitors, as well as captive customers of monopoly transmission providers, can obtain a continuous, reliable supply of power.

4 An excerpt from the FERC's 1981 Study of Power Pooling, which summarizes the economic and reliability benefits of coordination among utilities, is attached as Exhibit A.

Today, all transmission systems in the contiguous states are interconnected with other systems. Each is acutely and continuously affected by power flows on adjoining systems within three major, regional girds. The U.S. Supreme Court recognized the tight integration of these interconnections in its 1972 decision affirming federal jurisdiction over Florida Power & Light Co. because the interconnection of its Florida transmission system with transmission systems in other states caused its power to commingle with the power of others in interstate commerce. These integrated grids provide flexibility to utilities serving end-use consumers, large and small. Unlike the beginning of the twentieth century, when a utility's only source of supply was one or two nearby, interconnected generators, today's utilities can obtain energy and reserves required to backstop service reliability either locally or from generators many states removed. Indeed, many utilities providing service to end-use consumers C including most municipally owned and many cooperatively owned systems C have service obligations that far exceed the generating capacity that they own, making it necessary for them to depend on generation owned and operated by others as well as access to transmission systems interconnecting them with those generators.

A single, standardized set of open-access rules for using the interstate transmission grid on a nondiscriminatory basis maximizes opportunities for obtaining the economic and reliability benefits of coordination, which are reflected in the quality and price of service to end use consumers. Rather than operating on a stand-alone basis, with access only to one or two proximate resources to provide reliable service, today's electricity service providers can and do call on diverse portfolios of resources to guarantee service reliability. By allowing states to set different access rules for the majority of the transmission grid's capacity within their borders so that indigenous transmission owners can prioritize transmission service in support of their own in-state sales, section 101(b) of H.R. 2944 reverts to the isolated island misconception of the power industry and severely reduces the resources that any single service provider (especially municipal and cooperative systems) can rely on. In contrast, legislation enabling one regulator, at the federal level, to administer the rules of the road in a manner that is fair to all customers maximizes the opportunity to enhance reliability through coordination.

As an example of the reliability risks of the status quo, under FERC's existing regime that subjects only unbundled transmission to open and transparent access rules, the deleterious reliability and efficiency effects of the isolated island model became apparent in a reported incident from 1997. As recounted to FERC by Wisconsin Public Power, Inc. ("WPPI") and reported in FERC's Order No. 2000, a large and important transmission facility (345 kilovolt) became overloaded and automatically disconnected from the grid. The disconnection, in turn, caused "the transmission system over a large region to come perilously close to blackout." WPPI complained that neither it nor its neighboring systems were able to avert or manage this emergency properly because transmission owners were not subject to FERC open access and transparency rules in connection with their service to their own native load customers and consequently none of them knew how each other was causing power to flow within the regional grid. In this instance the failure to apply standardized federal open access and transparency rules to bundled transmission not only imperiled reliability, but it also lessened efficiency because, as WPPI explained, the lack of transparency causes transmission system operators "to make overly conservative, but inaccurate assumptions which unnecessarily reduce the amount of transmission capacity available to the market."

B. ***Regional Transmission Organizations.*** The Bill basically eliminates the authority proposed in the Discussion Draft, and widely-called for in other legislative proposals, respecting the FERC's authority to require participation in RTOs. Section 103 of the Bill amends section 202 of the Federal Power Act to provide that FERC is given no authority to compel a transmitting utility to join an RTO; instead, the FERC is mandated to approve applications by transmitting utilities to join an RTO, if the FERC determines that the RTO meets the specified standard. FERC is expressly prohibited from requiring a transmitting utility that applies to join a complying RTO to join a different RTO; moreover, FERC is required to permit an applicant to join an RTO to withdraw from the RTO if the FERC decides to impose terms or conditions other than those proposed by the applicant.

This version of RTO legislation leaves FERC without any authority to compel utilities to participate in RTOs. We note that the FERC's final rule on RTOs interprets several Federal Power Act provisions (including sections 203, 205 and 206) as granting FERC the authority to compel a utility to participate in an RTO. However, the enactment of Section 103 will no doubt be used to argue that since Congress expressly addresses the topic of RTOs in new Section 202 of the FPA, and therein denies FERC the authority to mandate participation, Sections 205 and 206, which do not expressly address this topic, cannot be relied upon as a grant of authority in this area.[5] Thus the Bill would represent a significant reduction in the authority of the FERC to insure non-discriminatory uses of the nation's bulk transmission system and would constitute a major retreat from the status quo. The result would be that many utility and utility holding company systems would continue as non-participants in an RTO, and transmission customers seeking to use their systems would continue to encounter "pancaked" transmission rates and would continue to suffer from the absence of the regional transmission planning and operating benefits that could be provided by an RTO. These circumstances, in turn, would adversely affect the development of the competitive energy commodity market and reduce the advantages that consumers might otherwise obtain from unconstrained competition among sellers.

In summary, the Bill's undermining the FERC's authority to require transmitting utilities to participate in RTOs, combined with its mandate that FERC's open access policies not apply to the transmission component of bundled retail sales and the lack of a mandate for open retail access, constitutes a "triple-whammy" against the creation of competitive markets for electricity in the U.S. Under the Bill, utilities that seek to use the monopoly power associated with their transmission

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[5] *See* the letter of December 23, 1999 from FERC Chairman Hoecker to Hon. Edward T. Markey, at p. 2.

facilities to advantage their own generation sources would be permitted to do so, with respect to their bundled retail sales. In addition, because there is no mandate to provide retail access, these utilities would be permitted to maintain their position as the franchised monopoly retail supplier and to deny access to others who would provide competition for retail sales. Finally, since FERC cannot require RTO participation, these utilities would be permitted to operate their transmission systems on an insular basis, which maintains pancaked transmission rates. This result would represent a significant backwards step in achieving the benefits that fair competition could provide to consumers.

2. Consumer Disclosure

Section 3 of the Bill provides that any state law adopted up to three years after the enactment of the Bill which addresses any matter addressed by, among other provisions, Title III of the Bill (the Consumer Protection provisions, including the Consumer Disclosure section), will displace the federal law provision. (The other provisions subject to "state law preemption" are section 532, the interconnection provisions for distributed generation, the aggregation provisions, section 531, and section 702, the net metering provision.) While paragraph 301(b)(2) of the Bill provides that both federal and consistent state law are to apply to disclosure of generation sources and emissions, the Section 3 grandfathering provision would displace federal law with state law. As discussed below, given the regional nature of the electricity market, the opposite approach -- namely an exclusive, uniform, federal standard -- should be adopted.

A. ***Emissions Information.*** Section 301 establishes a well-intentioned but impractical approach to consumer disclosure for generation sources for sales of both retail and wholesale power. Retail and wholesale sellers, including power marketers, would be required to provide, for every sale, a vast amount of information, including "the share of electric energy that is generated by each type of energy generation resource," and information regarding emissions, as required by the FTC. In today's trading markets, which involve multiple wheeling transactions, substitution of generation sources when primary sources are unavailable, and computer-speed transactions, it is either impossible, or extremely expensive, to obtain and provide this type of information; and while the Bill limits the FTC's requirements to those that are "technologically and economically feasible to provide," it is Enron's experience that some policy makers may not appreciate the technological problems and costs associated with implementing such an approach. However, the goal of this provision, to inform consumers as to the type of generation sources that are available and to encourage consumers to select more socially desirable generation, can be much more efficiently accomplished through a "certificate" approach. That approach, which is being tested by the Automated Power Exchange in California, offers the opportunity for generators to obtain certificates for various types of generation, and to send appropriate price signals to consumers by permitting trading of the certificates without the need to attempt to trace the actual flow of electrons from the generator to the load. This approach accomplishes the consumer disclosure goal while not interfering with the wholesale power market or trading in that market.

B. ***<u>Price Information</u>.*** In addition, paragraph 301(b) requires the FTC to impose specific requirements regarding pricing to be included in a statement that retail electric suppliers must provide to retail consumers. Enron retail affiliates engage in many transactions in which, for example, electric requirements are provided at a single "all-in" price (<u>e.g.</u>, $1 million/year to provide all the energy needs of an industrial facility). A requirement that the price of all charges associated with providing such service, such as "access charges, exit charges, back-up service charges, and customer service charges" would be extremely burdensome and would be irrelevant in this context.

C. ***<u>Uniform National Standard</u>.*** As in other industries that have been subjected to varying regulations by different states, subjecting retail suppliers to regulation by the FTC, and allowing the states to impose additional requirements (see paragraph (e) of Section 301) could make compliance extremely expensive. In the retail supply business, a key goal is for marketers to be in a position to serve many locations of a commercial or industrial customer pursuant to a single master contract and to use standardized billing. In this era of instantaneous transfer of the product hundreds of miles across many state borders, a preemptive uniform national standard should be relied upon to provide appropriate disclosure to consumers while not undermining the goal of consumers to reduce the costs of the product they are purchasing. While paragraph (e) requires that standards adopted by individual states not be inconsistent with the Bill or with the FTC's rules, there is a significant risk that those not involved in the nuts-and-bolts of trading will, for example, not consider multiple layers of state laws to be inconsistent with federal standards. In fact, given the multi-state nature of today's energy trading markets, the burdens of complying with numerous state laws, in addition to federal law, would constitute a substantial obstacle to the functioning of competitive markets. Finally, as noted above, application of the "state law preemption" approach set forth in Section 3 of the Bill would result in the absence of a uniform federal standard and the adoption of a "crazy-quilt" of inconsistent state laws, a result that could significantly disrupt the functioning of the interstate power market.

3. PUHCA Repeal

As noted above, with the elimination of a "date certain" for open retail access, failure to provide explicit authority for FERC to compel transmitting utilities to participate in an RTO, and the reservation of jurisdiction over the transmission component of bundled retail sales to the States, *the Bill has eliminated virtually all of the "carrots and sticks" for "closed" states and their utilities* to provide open retail access. Several large registered holding company systems which are supportive of PUHCA repeal as a way to expand their utility and non-utility businesses, continue to provide monopoly franchised retail service in a multitude of closed States, thus foreclosing competition in a large portion of the nation. To incentivize these States and holding companies to enable competition to benefit their retail consumers, PUHCA repeal should be conditioned, as provided in the Markey Amendment, so as not to apply to holding company systems with operating utility subsidiary companies in two or more "closed" states. Under this approach, holding companies which behave as they did in the pre-competition era will have to live with the regulatory framework that Congress determined was necessary to prevent the opportunity for investor and consumers abuses that occurred in that paradigm. Should these holding companies welcome competition by providing open access in most of the States in which their utility subsidiaries provide retail service, they will be freed from the constraints of PUHCA .

With respect to the specific proposals, with the above-noted caveat, Enron supports PUHCA repeal; however, the proposal in Section 511 would increase the regulation to which "exempt" holding companies, such as Enron Corp., are subjected, while virtually eliminating the pervasive regulation to which "registered" holding companies are subjected. This anomalous effect results from the increased access to books and records and authority to require record keeping granted to State commissions and to FERC. First, it makes no sense that the regulation to which exempt holding companies are subjected should increase as a result of PUHCA repeal. Second, even if such authority were to be expanded, the FERC's and State commissions' authority should be limited to the specific affiliate that transacts with a regulated utility; as now drafted, the legislation would permit State commissions to review books and records of entities that are engaged solely in unregulated activities and have no interaction with a regulated electric or gas utility company.

Also, under current law, a company whose sole utility assets or subsidiaries are qualifying facilities, exempt wholesale generators, and/or foreign utility companies (an "IPP Company"), does not become a holding company under PUHCA. However, the Bill, in section 505, would treat such a company as a holding company and would require FERC to issue a rule exempting such companies from Section 503 of the Bill, which requires FERC access to holding companies' books and records. Moreover, the FERC exemption would not even apply to state commission access to books and records under Section 504. As a consequence, IPP Companies, which heretofore have been exempt from state and federal utility regulation would, as a result of the repeal of PUHCA, become subject to significant additional state and, depending on FERC's final rule, federal regulation. This provision should be amended to exclude, by statute, IPP Companies from classification as a holding companies under Subtitle A of Title IV of the Bill.

4. Consumer Privacy and Metering

As noted previously, Section 3 of the Bill provides that if, in the time frame ending three years after enactment, a State law or regulation "addresses" any of several specified matters, including consumer privacy, addressed by the Bill, the State law displaces federal law. This approach will render virtually meaningless much of the privacy provisions, in that those states that protect consumers rights and insure that all competitors have equal access to crucial billing data have already enacted such state laws, whereas states that do not support consumers' privacy or retail competition are given a three-year window in which to enact legislation which merely "addresses" these subject matters and the federal law will cease to apply. Enron believes that the consumer privacy and competitive access goals of Section 302 are far too important to permit them to be rendered meaningless by Section 3.

With regard to the substantive provisions, Enron supports Section 302, which requires the FTC to adopt rules relating to preserving the privacy of consumer information. Enron also urges the inclusion of provisions guaranteeing to consumers the right to install, or to select a competitive supplier to install metering, so that consumers have the ability directly to determine the appropriate treatment of data concerning their own load data; however, provisions should be added to provide that, irrespective of who owns a customer's meter, procedures are available pursuant to which potential competitive retail suppliers can obtain access to information regarding customer usage patterns, provided that commercial and industrial customers must be permitted to restrict access to information that could provide sensitive information to competitors.

5. Expansion of and Eminent Domain for Transmission Facilities

Section 105 amends the FPA to permit FERC to order utilities to expand transmission facilities. This requirement confirms and expands the same requirement that is now in FERC Order No. 888. However, Enron recommends that the legislation also include a provision granting FERC-certified transmission projects the power of eminent domain, so as to enable such projects to proceed more expeditiously. The requirement for such authority is based on the fact that the key obstacle to expansion of utility transmission systems is the requirement to obtain individual permits or approvals from each State, and many local jurisdictions, in which the lines are being constructed. This is especially problematic if a line is planned through one State, but the beneficiaries of the line are in another. Enron accordingly recommends an approach similar to that established by Section 7 of the Natural Gas Act. In that statutory scheme, the FERC has the authority to certificate interstate pipeline facilities. The certificate enables the pipeline to exercise the power of eminent domain. Authorizing FERC to function similarly on the electric transmission side, including granting certificates to appropriate transmission projects, along with the power of eminent domain, is required if any real progress is to be made in alleviating transmission constraints. We note that one advantage of PUHCA repeal, as provided in Title V of the Bill, is that the PUHCA barriers associated with the creation of stand-alone transmission companies ("transcos") would be eliminated. In order to enable new transcos to benefit from the new eminent domain authority, the FERC's certification authority should be available to "start-up" transcos. One approach would be to confirm the status of a transco whose transmission rates have been accepted for filing under Section 205 of the FPA as a "public utility" that may be granted certificate authority.

6. Bonneville, TVA, and Other PMA's

Enron supports putting all transmission under FERC's jurisdiction in order to further the goals of open access and competition. This should apply equally to all Federal facilities, including the Bonneville Power Administration (BPA), the Tennessee Valley Authority (TVA), and the other power marketing administrations (PMAs). The Bill does not address the TVA issues, so Enron is reserving comment as to specifics of TVA restructuring.

Title VI, Subtitle B, proposes to place BPA's transmission function under the Federal Power Act subject to FERC's authority. We support this effort but disagree with the many proposed exemptions to this jurisdiction. These exemptions should be deleted because they are aimed at placating certain regional interests and thereby undermine the benefits of full FPA regulation for the majority of BPA transmission customers. These exemptions are conspicuously absent from the draft TVA subtitle being circulated by Rep. Ed Bryant and from Subtitle C, which addresses the other PMAs.

Enron opposes a surcharge on BPA's transmission service to recover shortfalls in BPA's power business line's costs for two reasons. First, the surcharge would force competitors of BPA's power business to subsidize BPA's power business line's sales. Second, the Bryant draft TVA subtitle includes no similar provision. Rather, the subtitle would have the FERC promulgate regulations to provide for stranded cost recovery (as determined by the FERC) from any departing customer that caused the stranded costs to be incurred. This is consistent with Order No. 888's requirements; the same principle should apply to BPA as well. It would force BPA to submit any subsidies of its power business to public scrutiny before FERC under the same standards the FERC has imposed on investor-owned utilities.

7. Incentive Rates for Transmission

Section 105 of the Bill amends the Federal Power Act by adding, among other things, Section 217, which addresses incentive rates for transmission. Section 217(a) of the FPA would permit transmitting utilities to recover costs of enlarging transmission facilities; however, notwithstanding the requirement in paragraph 217(c)(1) that rates be "just and reasonable," the language of Section 217(a) implies that cost recovery is permitted for all transmission costs, regardless of whether they, for example, reflect significant cost overruns caused by management imprudence. Paragraph 217(b) requires FERC to take into account "the incremental cost and benefit to interconnected transmission systems of such facilities." If, for example, a transmission line costs $10 million but provides benefits of $100 million, this language might be construed as requiring that rates be set anywhere in the $10-$100 million range. Because transmission facilities are generally viewed as "essential facilities" with monopoly characteristics, transmission owners traditionally have not been permitted to capture the monopoly rents associated with deregulated pricing. A preferable approach would be to require the FERC to find that there is "effective competition," as provided for in proposed FPA Section 217(f), discussed below, as a condition to permitting rates in excess of cost.

Section 217(e), which would permit transmission owners to charge negotiated rates, may provide incentives for transmission projects to be constructed in scenarios where traditional utility ratemaking techniques might have failed to provide the appropriate reward associated with the risks of the investment. However, vertically-integrated electric utilities historically had significant motivation to hinder competition with their merchant function by offering only one-sided "negotiated" transmission contracts to their captive wholesale customers, and the FERC, under its Section 206 authority to revise rates so as to render them "just and reasonable," often found it necessary to revise the rates, terms or conditions of these "negotiated" arrangements to overcome utility market power. It is not clear that Section 217(e) would permit this type of adjustment; indeed to do so would appear to be contrary to the purpose of this provision.

Section 217(f) permits the FERC, on a finding that the relevant geographic and product markets for transmission services or for delivered wholesale power are "subject to effective competition," to permit transmitting utilities to charge market-based rates for transmission. While the restriction limiting market-based rates to competitive circumstances is sensible, it should be limited to situations in which there is effective competition for transmission. That there is a competitive market for *generation* does not prevent a transmission owner from charging higher-than-market clearing prices, which, in turn, results in a suboptimal allocation of society's resources. Conversely, if a potential transmission customer is able to select from among several transmission providers, the threat of competition will effectively constrain the market-rates that the transmission owners can charge.

8. Mergers and Divestitures

Enron notes that the Bill does not contain the "divestiture" provision, which the Administration Bill and several other electricity restructuring bills contain, and which gives FERC the authority to compel divestiture based on a finding of market power and the ineffectiveness of other remedies to alleviate such market power. In order to insure that the acquisition of market power by participants in the bulk power markets does not undermine the intended results of this program, the legislation should be amended to provide FERC authority to require divestitures, where market power cannot effectively be eliminated through less intrusive measures, such as denial of the authority to sell power at market based rates.

Also, Section 402 of the Bill amends Section 203 of the Federal Power Act, which governs mergers and sales of jurisdictional assets, by imposing a 180 day deadline for FERC action. First, as a drafting matter, although it appears that the drafters intend to force FERC to act within 180 days by permitting such transactions to occur without prior FERC approval, following the 180 day period, new Section 203(a)(2) does not make clear what happens if the FERC fails to act within that period. Second, this provision mandates that FERC , if it makes the requisite findings, "approve" the transaction. In many instances, FERC has found it necessary to impose conditions on proposed mergers and acquisitions, in order to render then acceptable. The "shall approve" language here raises questions regarding the continued availability of that process.

More importantly, in merger cases raising complex substantive issues and involving numerous parties, 180 days following filing is simply too short a time period to complete discovery necessary for an effective hearing, the hearing itself, which may be required by the Administrative Procedures Act if there are material disputed issues of fact, and briefing to the administrative law judge and the full Commission. A legislative mandate to shorten the period for decision-making to an unrealistic time-frame is counterproductive, in that it may lead the FERC to deny applications with which it has questions, rather than risk approving them based on an inadequate record. On the other hand, a one-year deadline is more realistic and still would serve to expedite cases which have taken more than that time. Finally, as a procedural matter, the clock is started by the filing of an application. In order for this approach to work effectively, FERC, in other areas, such as QF filings, has been at times able to circumvent deadlines by deeming applications to be "incomplete" and therefore not accept them for filing. This provision should be amended to require FERC to establish clear guidelines on what must be included in an application and to prohibit FERC from rejecting an application that contains the required information.

9. Interconnection Procedures

Section 532 of the Bill contains several favorable changes to the FPA's interconnection provisions. First, paragraph 532(a) adds new Section 210(f) to the FPA, which requires that local distribution companies interconnect with distributed generation facilities, *i.e.*, facilities that provide "inside-the-fence" service and export or import additional power. Also, the FERC is required to issue rules establishing uniform standards relating to safety, reliability and power quality standards for interconnection of distributed generation facilities. These provisions, if binding, would go far toward enabling on-site generation to compete in the marketplace by enabling them to obtain access at the grid at the distribution level. However, as noted above, Section 532 is subject to the "any state action within three years of enactment preemption" of Section 3 of the Bill, which means that a State could enable a franchised utility to maintain the ability to thwart competition by adopting legislation or regulations that "address" this topic (presumably including prohibiting, or very limiting, its availability). To avoid this result, Section 532(a) should be exempted from the State preemption standard of Section 3 of the Bill.

Second, Section 532(b) would permit a "transmitting utility" to be an applicant for an interconnection order. In conjunction with the change to the definition of "transmitting utility" in Section 102(c) of the Bill, which eliminates the requirement that a transmitting utility's facilities be "used for the sale of electric energy at wholesale," this change enables a transco to apply for interconnection. The Bill adds "transmission utilities" to the universe of entities that may be the target of an interconnection order. Also, the Bill eliminates the requirement for an "evidentiary hearing" and the prohibition on interconnection orders relating to Federal power marketing agencies.

However, these changes do not enable FERC to order interconnection at the distribution level and do not enable distribution-only utilities to be applicants for an interconnection order. (The above-described distribution generation provisions would at least partially provide the answer, but they are subject to State veto.) Today, many innovative customer or energy service provider facilities are located on a utility's distribution system and may be many miles away from a higher-voltage transmission interconnection point. While the Bill would enable FERC to require expansion of the distribution system in order to accommodate a transmission-level interconnection, it would not enable an applicant to apply for an interconnection at the distribution level. This omission is likely to lead either to the failure to pursue otherwise viable innovations or to require customers needlessly to construct facilities necessary to reach an interconnection point at the transmission level. To avoid these problems, the universe of interconnection targets in Section 210(a)(1)(A) of the FPA should be expanded to include the distribution facilities of an electric utility or a transmitting utility.

Also, the class of applicants should be expanded beyond its present limited nature to include any "person" as defined in the FPA. There is little remaining policy justification for allowing any "electric utility, Federal power marketing agency, geothermal power producer . . ., qualifying cogenerator, or qualifying small power producer" to be an applicant, and excluding customers seeking interconnection that happen not to fit within one of these specific categories.

10. Export and Import of Power

Section 202(f) of the Federal Power Act provides that the ownership of transmission facilities used only for wholesale power sales (i) in which power is generated in a State (in the U.S.) and transmitted directly to a foreign country, without being transmitted through a second state, or (ii) in which power generated in a foreign country is transmitted into a State and not transmitted into a second state does not subject the owner or operator to FERC jurisdiction. This provision does not exempt from FERC jurisdiction companies that otherwise are subject to FERC jurisdiction; however, it would apply to a new "transco" whose sole activity was to own or operate transmission lines between the U.S. and a foreign country. Also, Section 201(c) of the Federal Power Act provides that transmission "in interstate commerce," meaning subject to FERC regulatory jurisdiction, is limited to transactions that take place within the U.S. The FERC has interpreted this provision of the Federal Power Act as granting it jurisdiction over the portion of a export or import transaction up to the border (and therefore subjecting those transactions to Order Nos. 888 and 889 procedures), but not the portion crossing the border or in a foreign country. The FERC has also concluded that it lacks the authority to order transmission service over "international lines." FERC has urged the Department of Energy, which has jurisdiction to issue permits to construct the interconnection at the border, to condition such permits on the utility's compliance with open access policies. [6]

Section 102(d) of the Bill would delete the above-noted limitation on FERC jurisdiction over transactions to or from foreign countries, thus enabling the FERC to require compliance with Order Nos. 888 and 889 on a utility's transmission lines all the way to the international border (i.e., including the portion of the line currently subject to DOE jurisdiction under Section 202(e) of the FPA). We recommend repeal of Section 202(f), so as to prevent discrimination by new transcos described above.

11. PURPA Repeal

In contrast to other versions of a PURPA repeal provision, which eliminate only the obligation to purchase from qualifying facilities, Section 521 also would repeal the requirement under Section 210(a)(1) of PURPA that electric utilities provide power to QFs, and the requirement of Section 210(c) that rates for utility service to QFs be just and reasonable and nondiscriminatory. These "sale" provisions are completely independent of the "must purchase" and "avoided cost" provisions of PURPA and the FERC's implementing rules. They simply mandate that utilities provide the back-up, supplementary, and other type of services needed to permit cogenerators and their customers to receive uninterrupted service. The FERC's rules implementing this Section simply require that in pricing such services, electric utilities not discriminate against QFs or their retail customers simply because of the fact that they receive a portion of their supply from on-site generation. These requirements are still necessary and appropriate, to insure that a key source of efficient energy production is not once again rendered unviable by virtue of anticompetitive behavior by franchised utilities, and thus should not be eliminated as part of PURPA repeal.

12. Retail Reciprocity

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[6] We note that on July 7, 1999, the Department of Energy issued proposed rules that would require applicants for Presidential Permits authorizing construction of transmission facilities crossing a U.S. border and for authorization under Section 202(e) of the FPA to provide open access. However, because this is still a proposed rule that could be altered in the final version or by a future Commission, it is preferable for this requirement to be enacted through legislation.

The Bill does not contain a retail reciprocity provision; however, efforts may be made to reinsert such a provision in the Bill. Enron opposes the inclusion of a retail reciprocity provision because of the potential of such a provision to eliminate much needed competitors from retail markets. Accordingly, Enron's first choice would be to continue not to include any reciprocity provision. If such a provision is included, we note that prior versions of reciprocity provisions, including Section 501 of the Subcommittee's Discussion Draft, prohibit a retail supplier that owns or controls, or has an affiliate which owns or controls, retail distribution facilities that are not "open" to retail access, from selling energy to retail customers in transactions involving local distribution facilities owned by another entity. Section 501 of the Discussion Draft proposed to add a new section of Section 219 of the FPA, which addressed the circumstance in which a distribution utility or an affiliated retail supplier has attempted to implement retail access on its system by filing a plan to provide open access with the relevant State commission. This provision appropriately sought to prevent an affiliated retail supplier from being held "captive" as a result of the policies of the State commission which regulates its affiliated utility. If this provision is re-adopted, to insure that it achieves the desired effect, it should be clarified that the filing of a plan to provide open access protects the affiliates of a distribution utility from being excluded from retail markets in other states, irrespective of whether the State commission with which such a plan is filed adopts, partially adopts or rejects the filed proposal. Also, the exception must apply irrespective of whether the open access plan was filed prior to the enactment of the new legislation.

Moreover, if a retail provision is added to the Bill, the retail reciprocity provision should be amended to provide a three-year phase in. This will provide utilities and State commissions adequate time to reassess their policies, in light of the potentially punitive effect of remaining closed to retail access.